

EX PARTE OR LATE FILED

RECEIVED



Communications Company, Inc.

GOVERNMENT AFFAIRS OFFICE
3000 K STREET, N.W., SUITE 300
WASHINGTON, D.C. 20007
TEL. (202) 424-7709
FAX (202) 424-7645

JUL 26 1996

FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF SECRETARY

DOCKET FILE COPY ORIGINAL

VIA COURIER

July 26, 1996

William F. Caton, Acting Secretary
Federal Communications Commission
1919 M Street
Washington, D. C. 20554

Re: Ex Parte Filing by MFS Communications Company, Inc.
in CC Docket 96-98

Dear Mr. Caton:

Yesterday, I became aware of the attached opinion of Scott Cleland, an industry analyst at *The Washington Research Group*. He speculates about the possible impact on competitive access providers (CAPs) of several possible decisions the Commission may reach in its pending interconnection proceeding. While we don't know which, if any, of these positions the Commission may adopt, I would like to bring his perspective to the attention of the Commission and ask that you consider the impact that such opinions, even though based on speculation, have on the business and financial market prospects of both incumbents and new entrants.

In this particular case, the analyst seems to have combined mutually exclusive possible decisions and concluded that if all happened, CAP business plans would be "knee-capp[ed]." Fortunately, the future of CAPs is no where near so dim. For example, MFS participates in the market as a facility based local service provider, as the largest ILEC service reseller, as an interexchange carrier and as an Internet provider. Our activities have already caused incumbent local carriers to restructure their rates -- particularly for dedicated high capacity digital facilities -- to the direct benefit of customers. Yet, we still profitably offer our services because we are an alternate, high quality supplier focused long term on facilities based platforms.

The Commission will reach truly industry-reshaping decisions as it adopts its interconnection order. It might well remember the lesson learned with interstate resale -- even without discounts, competitors can quickly rationalize incumbent pricing -- but only when all prices of an incumbent are disclosed and all services are subject to resale. As several competitors recently observed, no discount may be necessary if high volume local services such as Centrex are subject to unrestricted resale. Regardless of the discount level it finally adopts, the Commission should order that the discount apply to all ILEC services and that each ILEC must disclose all of its end-user pricing plans including individual case basis pricing just as they are required to disclose all inter-carrier agreements.

For the Commission
L. J. ABRAHAM

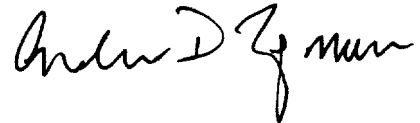
021

The Commission should order that network elements be defined and priced for each service or that a common set of network elements underlie all services with the network element prices imputed in the wholesale rate of each service. Since the incumbent will not know which services will be provided over which network element, a common set of network elements seems more plausible. Should an IXC, or any other new entrant, elect to lease network elements, the sum of prices for network elements leased from the ILEC coupled with the network elements the new entrant must provide for itself or procure elsewhere may exceed the service resale price. Of course, this calculus will be substantially effected by the number and definitions of network elements that the Commission also will decide in this proceeding

Finally, Mr. Cleland suggests the Commission will opt to encourage resale as a way of more quickly developing some competition for local service. Reliance on resale will not satisfy other objectives of the legislation that this docket is intended to implement -- development of widespread, effective, landline, facility-based competition. As Mr. Cleland observes, unduly deep discounts will discourage facility based competition. While this may delay RBOC entry into interexchange markets, it will also deter competitive opportunities to offer services based on new facilities.

For these reasons, MFS urges the Commission to order: relatively small resale discounts that encourage more rapid deployment of competing facilities; full disclosure of all ILEC end-user prices; and, a common set of network elements the prices of which are imputed to all ILEC services.

Very truly yours,



Andrew D. Lipman
Senior Vice President -
Legal and Regulatory Affairs

Attachment

cc: Chairman Hundt
Commissioner Chong
Commissioner Ness
Commissioner Quello
Regina Keeny
Robert Pepper

The Washington Research Group

A Division of Lynch, Jones & Ryan, Inc.

1000 Thomas Jefferson St. NW, Suite 606

Washington, DC 20007

Tel (202) 298-6226 Fax (202) 298-6146 Telex (202) 872-3557

Telecom/Cable Bulletin

Scott Cleland

July 24, 1996

Upcoming FCC Rules Big Trouble For CAPs

Summary: WRG is changing our strategic outlook for the Competitive Access Providers (CAPs) from positive to negative because of the local competition strategy WRG expects the FCC to employ in implementing the Telecom Act.

WRG cautions investors that upcoming FCC rules could eventually eliminate the CAPs' regulatory-protected niche, squeeze the CAPs' current subsidy arbitrage spread on which their current business is based, slow their growth potential considerably, impede their facility investment plans, and diminish any potential acquisition premium they may enjoy. The CAPs affected are: MFS (MFSST) Interstates (ICD), Tidewater (TCGI), Brooks Fiber, Intelecom Group (ICG) and any privately-held CAPs intending to go public.

Upcoming FCC Rules Negative For CAPs: It is now clear to WRG that the FCC's interconnection rules expected in early August will 1) have a strong tacit bias toward resale over protecting facilities-based competitors; and 2) allow long distance carriers to buy unbundled local loop elements and assemble them as a complete package without having to pay access charges; and 3) assume access charge reform by January 1997. (WRG expects the FCC to promote resale pricing guidelines which in the end result in effective average discounts approximating 22 percent for wholesale resale and roughly approximating 30-35 percent for unbundled resale.)

Because the Telecom Act is either ambiguous or silent on these matters, these FCC decisions fall into the "gray area" of FCC regulatory flexibility. Unfortunately for the CAPs, these FCC decisions have unmistakably negative repercussions for the CAPs.

Law Forces FCC to be Expedient: While the FCC has no desire to hurt the CAPs because the FCC for all practical purposes "birthed and nurtured" the CAP industry from infancy with protective regulations over the years, the new regulatory reality created by the Telecom Act requires the FCC to try to rapidly promote local competition nationally for residences and businesses.

It is becoming increasingly obvious to WRG that FCC has tacitly passed its hopes for rapid nationwide local competition on AT&T and MCI's ability to resell ("rebrand") local services. The FCC appears to have shrewdly concluded that: 1) much of the local

loop is indeed a natural monopoly for now, 2) neither the CAPs nor the cable industry has the financial or operational wherewithal for national residential and business competition; and 3) while it's not a good option to have to count on a long distance "rebrand" strategy working, it's the best option available within the legal constraints of the Telecom Act.

FCC "Ease-copying" the CAPs' Business Model: By changing the rules of the local competition game so dramatically mid-game, the FCC is effectively cutting off the CAPs business story at the knees.

A strong national resale emphasis:
develops alternative local facilities investment by making it unnecessary for an aspiring local entrant;

encourages AT&T and MCI to go around the CAPs and deal directly with the ubiquitous telcos rather than going through the tiny CAPs and paying their additional toll; and

turns the CAPs, in other words, into mere-sary "middlemen" whose profit on top of the telcos' cost and profit further squeezes the already tight resellers' margins (which WRG estimates will be on average 22-35 percent at best);

Access charge, bypass and reform: (and ultimately Universal Service subsidy reform making subsidies more explicit and theoretically competitively neutral);

undermines much of the original business case of the CAPs, which is predicated on the current subsidy arbitrage spread, thus forcing them to find new profitable revenue streams;

Makes "cream skimming" much harder because the cream will be going away eventually and many much bigger competitors will be vying to skim what's left; and

ends the CAPs' Universal Service subsidy "free ride" because the CAPs, like all carriers, will have to pay their fair share of the subsidy according to Section 254 of the new law. ***

WRG is a division of Lynch, Jones & Ryan, Inc. member NYSE and other regulated companies (212) 298-3117, telex (202) 872-3557. Information contained herein is based on data obtained from recognized official sources, issuer reports or communications, or other sources believed to be reliable. However, such information has not been verified by us, and we do not make any representation as to its accuracy or completeness. Any statements contained in this document are only current opinions, subject to change. Lynch, Jones & Ryan, Inc. is a privately held company and its securities are not registered with the SEC. This document is not intended to be used in any way to sell or to validate an offer to buy any securities mentioned herein. The firm (or persons related thereto) may perform investment